Homework 2 AP Economics Part 2 Chapter 10

1. Consider the following situations and determine whether they exhibit simultaneous consumption, network effects, x-inefficiency or rent-seeking behavior. Assume the businesses referenced function as monopolies.

(a) A pharmaceutical company discovers a vaccine for the common cold. The company puts a significant effort into tests to get it FDA-approved and into hiring lawyers to obtain a patent.

(b) An Internet service provider adds thousands of new customers.

(c) The head of a family-owned, major hotel chain decides to hire his wild, socialite niece to work as an executive of the company after her reality TV career ends.

(d) An online profile company helps college and high school students from across the country to connect with each other.

2. Explain the relationship between the price elasticity of demand and price discrimination. Give two examples.

3. In the table below are cost and demand data for a pure monopolist.

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Quantity demanded** | **Price** | **Marginal revenue** | **Average cost** | **Marginal cost** |
| 0 | $105.00 |  |  |  |
| 1 | 96.00 | $ 96.00 | $144.00 | $144.00 |
| 2 | 87.00 | 78.00 | 90.00 | 36.00 |
| 3 | 78.00 | 60.00 | 70.34 | 30.00 |
| 4 | 69.00 | 42.00 | 63.00 | 42.00 |
| 5 | 60.00 | 24.00 | 60.00 | 48.00 |
| 6 | 51.00 | 6.00 | 58.50 | 51.00 |
| 7 | 42.00 | –12.00 | 57.86 | 54.00 |
| 8 | 33.00 | –30.00 | 57.50 | 55.50 |
| 9 | 24.00 | –48.00 | 57.33 | 56.00 |

(a) What is the level of price, output, and amount of profit for an unregulated monopolist?

(b) Using the data in the table, what are the price, output, and profit for a regulated monopolist that sets price equal to marginal cost compared with an unregulated monopolist?

(c) Using the data in the table, what are the price, output, and profit for a regulated monopolist that charges a “fair-return” price compared with an unregulated monopolist?

(d) Analyze the effect of regulation on the allocation of resources. Which situation is most efficient? Which situation is most likely to be chosen by government? Why?

4. (Last Word) How was the original DeBeers diamond company an example of classic monopoly behavior?